



# **Legislative Audit Division**

**State of Montana**

**Report to the Legislature**

**November 2006**

## **Financial-Compliance Audit**

**For the Two Fiscal Years Ended June 30, 2006**

## **Office of the Secretary of State**

**This report contains six recommendations related to:**

- **Recording revenue and expenditures in accordance with state accounting policy.**
- **Compliance with federal grant requirements.**
- **Ensuring fees charged for business services are commensurate with the cost of providing those services.**

**Direct comments/inquiries to:  
Legislative Audit Division  
Room 160, State Capitol  
PO Box 201705  
Helena MT 59620-1705**

**06-19**

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## **FINANCIAL-COMPLIANCE AUDITS**

Financial-compliance audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2007, will be issued by March 31, 2008. The Single Audit Report for the two fiscal years ended June 30, 2005, was issued on March 6, 2006. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator  
Office of Budget and Program Planning  
State Capitol  
Helena MT 59620  
Phone (406) 444-3616

Legislative Audit Division  
Room 160, State Capitol  
PO Box 201705  
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# LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor  
Tori Hunthausen,  
Chief Deputy Legislative Auditor



Deputy Legislative Auditors:  
James Gillett  
Jim Pellegrini

November 2006

The Legislative Audit Committee  
of the Montana State Legislature:

This is our financial-compliance audit report on the Office of the Secretary of State for the two fiscal years ended June 30, 2006. Included in this report are recommendations to record revenues and expenditures in accordance with state accounting policy, comply with federal grant requirements, and ensure fees charged for business services are commensurate with the cost of providing those services. The office's written response to the audit recommendations is included in the back of the audit report, beginning on page B-3.

We thank the Secretary of State and his staff for their assistance and cooperation.

Respectfully submitted,

*/s/ Scott A. Seacat*

Scott A. Seacat  
Legislative Auditor

# **Legislative Audit Division**

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**Financial-Compliance Audit**

**For the Two Fiscal Years Ended June 30, 2006**

## **Office of the Secretary of State**

Members of the audit staff involved in this audit were Jeane Carstensen-Garrett, John Fine, Jim Manning, Sonia Powell, and Vickie Rauser.

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## **Elected and Administrative Officials**

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### **Office of the Secretary of State**

Brad Johnson	Secretary of State
Mark Simonich	Chief Deputy
Janice Doggett	Chief Legal Counsel
Jean Branscum	Deputy for Administrative Rules and Management Services
Mike O'Brien	Deputy for Business Services
Elaine Graveley	Deputy for Elections
Patti Borsberry	Deputy for Records and Information Management

For additional information concerning the Office of the Secretary of State, contact Brad Johnson, Secretary of State, at:

PO Box 202801  
Helena MT 59620-2801  
(406) 444-2034  
e-mail: [sos@mt.gov](mailto:sos@mt.gov)

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### Office of the Secretary of State

This financial-compliance audit report documents the results of our audit of the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2006. We issued a qualified opinion on the financial schedules of the office for fiscal years 2004-05 and 2005-06. This means the reader should use caution in relying on the financial information presented and the supporting detailed information on the state's accounting records.

This audit report contains six recommendations. The recommendations relate to recording revenues and expenditures in accordance with state accounting policy, complying with federal grant requirements, and ensuring fees charged for business services are commensurate with the cost of providing those services.

The prior audit report contained two recommendations. The office implemented one recommendation and partially implemented one recommendation.

The listing below serves as a means of summarizing the recommendations contained in the report, the office's response thereto, and a reference to the supporting comments.

#### Recommendation #1

We recommend the office record revenues and expenses associated with electronic business transactions in accordance with state accounting policy..... 4

Office Response: Concur. See page B-3.

#### Recommendation #2

We recommend the office properly classify federal expenditures in accordance with state accounting policy..... 5

Office Response: Concur. See page B-3.

#### Recommendation #3

We recommend the office provide the appropriate level of accounting expertise to its staff to ensure office transactions are properly recorded on the state's accounting system..... 6

Office Response: Concur. See page B-4.

## Report Summary

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### Recommendation #4

We recommend the office provide training and develop procedures to properly administer its federal programs. .... 8

Office Response: Concur. See page B-4.

### Recommendation #5

We recommend the office comply with state law by ensuring that fees charged for its business services reflect the cost of providing those services. .... 9

Office Response: Concur. See page B-4.

### Recommendation #6

We recommend the office comply with state law by providing the legislature information reporting state and UCC rule discrepancies. .... 10

Office Response: Concur. See page B-5.



# Introduction

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## Scope

We performed a financial-compliance audit of the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2006. The audit objectives were to:

1. Determine office compliance with selected laws and regulations.
2. Make recommendations for improvements in the management and internal controls of the office.
3. Determine the implementation status of prior audit recommendations.
4. Determine if the financial schedules present fairly the results of operations of the office for the two fiscal years ended June 30, 2006.

This report contains six recommendations to the office. Areas of concern not having a significant effect on the successful operations of the office are not included in this report but have been discussed with management. In accordance with section 5-13-307, MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations in this report.

We audited fees charged by the office to determine whether fees were commensurate with the overall costs of the office and reasonably reflected the prevailing rates charged in public and private sectors for similar services, as required by section 2-15-405(2)(a), MCA. We noted the office's fees were not commensurate with costs, as described on page 8 of this report.

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## Background

Article VI, section 1, of the Montana Constitution states the executive branch of state government includes a Secretary of State. Title 2, chapter 15, part 4, of the Montana Code Annotated sets forth the Secretary of State's duties. The office has 54.25 FTE in four divisions and the executive office. The office files, stores, maintains, and preserves permanent records of the state and certain public interest records of private citizens. The office publishes the Montana Administrative Register (MAR) and the Administrative Rules of Montana (ARM). The office is also responsible for the commissioning of Notary Publics in Montana.

## **Introduction**

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The Secretary of State serves as chief election officer for the state, maintaining uniformity in the application of the election laws and retaining election records through the Elections Bureau. In addition, the Secretary of State serves as a member of the Board of Land Commissioners and the Board of Examiners.

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### **Prior Audit Recommendations**

We performed the prior audit of the office for the two fiscal years ended June 30, 2004, which contained two recommendations to the office. The office implemented one recommendation and partially implemented one recommendation. The partially implemented recommendation, which related to providing adequate supervision and training for the office's accounting function to ensure compliance with state law and accounting policy, is discussed again on page 5 of this report.

# Findings and Recommendations

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## Accounting Errors

During our financial-compliance audit of the Secretary of State's office, we tested revenue and expenditure transactions to determine if amounts recorded on the accounting system were reasonable and adequately supported by receipts, invoices, or other acceptable documentation. For costs related to the Help America Vote Act (HAVA), which were over \$4 million in the fiscal year ended June 30, 2006, we also determined if the amounts paid to the various subrecipients were consistent with goals identified in the office's state HAVA plan and in accordance with federal regulations.

The following sections document instances where the revenue and expenditure amounts reviewed were not recorded correctly on the state's accounting system.

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## Montana Interactive Fees

**The office did not record the revenues and fees associated with electronic business filings.**

The office contracts with Montana Interactive, LLC (MI) to perform electronic business services using the Internet. As part of this contract, MI retains a portion of the revenue received to pay for the services it provides to the office (service fees) and for fees charged for the acceptance of the electronic form of payment (i.e., debit or credit card). The net amount of revenue is then remitted monthly to the office. For example, a \$15 annual report filing is reduced by the \$2 service fee and \$1 electronic payment fee, resulting in a net amount remitted to the office of \$12.

During fiscal years 2004-05 and 2005-06, MI charged the office \$216,421, and \$338,399, respectively, for service and electronic payment fees. The office only recorded the net amount of revenues remitted by MI. As a result, Charges for Services revenues and Other Services expenses in the office's Enterprise Fund are understated by \$216,421 in fiscal year 2004-05 and by \$338,399 in fiscal year 2005-06.

## Findings and Recommendations

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State accounting policy requires the office to record the full revenue charged with an off-setting expense for the amount of the collection fee. Accounting staff was not aware of the requirement to record the revenues and collection costs to appropriately reflect the activity associated with this contract. In February 2006, we notified the office staff that they needed to record this information on their accounting records, and at that time, the office contacted MI to obtain the dollar amount of these fees. However, staff did not follow up with MI concerning the information requested, nor did staff record estimated fees to approximate actual charges withheld by MI. When the information was finally received on July 21, 2006, the 2005-06 fiscal year-end closing process had already been completed.

As described in our Independent Auditor's Report on page A-3, the omission of these fees misstated the Charges for Services revenues and Other Services expenses shown in the financial schedule presentation. This resulted in an opinion qualification for the Schedules of Total Revenues & Transfers-In and the Schedules of Total Expenditures & Transfers-Out for each of the two fiscal years ending June 30, 2006.

### **Recommendation #1**

**We recommend the office record revenues and expenses associated with electronic business transactions in accordance with state accounting policy.**

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### **Grants from Federal Sources Misclassification**

#### **The office made errors when recording federal expenditures.**

In fiscal year 2004-05, the office recorded \$852,322 in county payments and reimbursements made under HAVA as Other Services, Supplies & Materials, Other Operating Expense, and Grants from State Sources. The correct classification for these payments, according to state policy, was Grants from Federal Sources. Accounting staff incorrectly assumed that payments for equipment and training were part of the office's costs, even though these

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## Findings and Recommendations

payments were being made on behalf of the counties benefiting from the HAVA program. Payments shown as Grants from State Sources were misclassified, due to a staff coding error.

In fiscal year 2005-06, the office recorded \$4,677,545 in county payments and reimbursements made under HAVA as Grants from State Sources, instead of the correct classification of Grants from Federal Sources, as required by state accounting policy. Staff explained that this misclassification was also due to a coding error.

As described in the Independent Auditor's Report on page A-3, the cumulative amount of the above coding errors misstated the Grants from Federal Sources classification shown on the financial schedule presentation, resulting in an opinion qualification for the Schedules of Total Expenditures & Transfers-Out for each of the two fiscal years ended June 30, 2006.

### **Recommendation #2**

**We recommend the office properly classify federal expenditures in accordance with state accounting policy.**

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## Summary

**The office has not fully implemented our prior audit recommendation.**

Each of the four previous financial-compliance audit reports have all contained recommendations related to appropriately recording office transactions on the state's accounting records. The types of issues noted in these audits ranged from appropriately allocating costs between the Enterprise and Internal Services Funds, recording payroll, equipment, and software purchases expenses when incurred, unrecognized revenues related to business services receipts, duplicate revenue entries related to prepaid accounts, and overstated revenues and expenses related to records management fees.

Our prior audit recommended the office provide adequate supervision and training for the office's accounting function to

## Findings and Recommendations

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ensure compliance with state law and accounting policy. The office concurred with our recommendation, arranging for training opportunities for its accountant and hiring a supervisor to oversee operations for the Management Services Division. Due to the nature of the accounting errors noted in the above report sections, however, and the consistent accounting errors identified in the prior four financial-compliance audits, we believe that additional expertise is needed to alleviate problems with properly recording revenue and expenditure transactions on the state's accounting system.

### **Recommendation #3**

**We recommend the office provide the appropriate level of accounting expertise to its staff to ensure office transactions are properly recorded on the state's accounting system.**

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### **Federal Compliance**

**Payments made to a nonprofit organization were not adequately documented, advertising costs were not put out for bid, and financial status reports did not reconcile to the accounting system.**

Funds received under federal programs, such as HAVA and Election Assistance for Individuals with Disabilities (EAID) programs, are subject to various federal compliance requirements, including requirements relating to allowable activities, allowable costs, procurement, and reporting guidelines.

The following three sections identify situations where the office did not comply with some of these requirements.

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### **Unsupported Payments**

During fiscal year 2004-05, the office received a \$100,000 grant from the EAID program, which was used to conduct polling place accessibility surveys for voters with disabilities. In its federal grant application, the office proposed to contract with a local nonprofit organization to provide these services.

## Findings and Recommendations

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During our audit, we reviewed \$68,000 paid to the nonprofit in fiscal year 2005-06. We noted that although the nonprofit invoiced the office for services provided, there was no documentation to support whether the amounts paid were allowable under the grant regulations. As a result, we question \$68,000 in EAID funds paid to the nonprofit organization.

Without additional documentation, such as a subgrant specifying the services to be performed, the office does not have support to demonstrate that the nonprofit conducted its activities in accordance with the representations made to the federal government in the grant application. Staff explained that prior legal counsel did not prepare a contract.

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### Financial Status Reporting

Each year, the office is required to submit financial and narrative status reports to the federal Elections Services Commission describing its use of the HAVA funds received. During our audit, we reviewed two of the financial and narrative reports submitted and noted that the amounts on the financial status report did not reconcile to the amounts on the accounting records. When staff reviewed the reports they submitted to the federal government, and reconciled the reported amounts to the financial records, they found a \$131,000 error in the amount of expenditures previously reported to the federal government.

Federal reporting requirements specify that amounts reported for federal grants reflect the use of all funds and reconcile to amounts shown on the accounting system.

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### Questioned Costs for HAVA Advertising

In fiscal year 2004-05, the office published a series of informational advertisements in local newspapers to describe voting procedure changes. The office paid \$27,728 to one vendor, and \$51,182 to a separate vendor, for these advertisements.

Federal procurement requirements direct grant recipients to follow state purchasing policies for purchases made with federal funds. State policy requires payments for goods or services in excess of

## Findings and Recommendations

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\$25,000 either be put out for a competitive bid or have sole source documentation.

Staff explained that these advertisements were authorized by the prior Secretary of State administration. As of September 20, 2006, the office has worked with the state's Procurement Bureau to solicit and award bids for upcoming advertisements. However, because the office paid for the prior advertising services without following state procurement policy, we question \$78,910 in advertising costs paid from federal funds.

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### Summary

Prior to fiscal year 2002-03, the office did not administer any large federal grant awards. Unfamiliarity with federal compliance requirements led to some of the problems noted in the above report sections. The office needs to develop procedures, and train its staff, to ensure proper oversight for the federal programs it administers.

#### **Recommendation #4**

**We recommend the office provide training and develop procedures to properly administer its federal programs.**

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### State Compliance

The following report sections identify two instances where the office did not comply with state laws.

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### Enterprise Fund Fees

#### **Fees are not commensurate with the costs in the Enterprise Fund.**

Section 2-15-405(2)(a), MCA, requires that the office charge fees that reflect the cost of providing its various business services. During our audit, we reviewed activity for the Enterprise Fund and noted the fund equity had increased each year of the audit period, from \$2,516,189, to \$3,103,735 to \$3,893,786 at June 30, 2004, 2005, and 2006, respectively. Fund balance is a reflection of the excess of revenues over expenses, as well as ending assets and liabilities.



## Findings and Recommendations

The following information documents revenue and expense amounts for the two fiscal years ended June 30, 2006:

<b>Enterprise Fund</b>		
<b><u>Revenue and Expense Amounts</u></b>		
<b><u>for the Two Fiscal Years Ended June 30, 2006</u></b>		
<b><u>Fiscal Year</u></b>	<b><u>2005</u></b>	<b><u>2006</u></b>
<b>Revenues</b>	\$ 3,744,722	\$ 4,006,263
<b>Expenses</b>	<u>3,152,947</u>	<u>3,216,212</u>
<b>Excess Revenues</b>	\$ <u>591,775</u>	\$ <u>790,051</u>
<b>Ending Fund Balance</b>	\$ 3,103,735	\$ 3,893,786

**Source: Compiled by the Legislative Audit Division.**

Office staff indicated that updating their existing computer databases, and implementing new programs, will absorb the fund balance of \$3,893,786

Despite the fact that the office may have a need to make capital improvements in the future, statute does not allow provisions to accumulate fund balance in anticipation of future purchases. The office needs to examine the costs associated with its various business services, and take into consideration current fund balance, in order to set rates that are commensurate with the costs of providing the service.

### **Recommendation #5**

**We recommend the office comply with state law by ensuring that fees charged for its business services reflect the cost of providing those services.**

### **Compliance with Duty to Report Requirements**

**The office did not file Uniform Commercial Code rule discrepancy reports with the legislature, as required by state law.**

As part of its duties, the office processes and records lien filings for security interests using the Uniform Commercial Code (UCC) as

## Findings and Recommendations

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guidance for these transactions. Effective July 1, 2001, the state adopted a revised version of the UCC model rules, as did various other states, in order to help promote consistency in interpreting and applying the various requirements under UCC guidelines.

Section 30-9A-527, MCA, directs the office to report to each legislature all instances where its rules differ from the UCC model rules. During our audit, we found that the office had not provided this information to the 2005 Legislature, although staff had identified four instances where the office's rules, or state law, were not consistent with the UCC model rules.

### **Recommendation #6**

**We recommend the office comply with state law by providing the legislature information reporting state and UCC rule discrepancies.**

# **Independent Auditor's Report & Office Financial Schedules**

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# LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor  
Tori Hunthausen,  
Chief Deputy Legislative Auditor



Deputy Legislative Auditors:  
James Gillett  
Jim Pellegrini

## INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee  
of the Montana State Legislature:

We have audited the accompanying Schedules of Changes in Fund Balances/Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Office of the Secretary of State (office) for each of the two fiscal years ended June 30, 2006, and 2005. The information contained in these financial schedules is the responsibility of the office's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, the financial schedules are presented on a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The schedules are not intended to be a complete presentation and disclosure of the office's assets, liabilities, and cash flows.

The office did not record costs associated with electronic processing of business services fees charged to the office by Montana Interactive during fiscal year 2004-05 and fiscal year 2005-06. The omission of these fees resulted in understated revenues and expenses of \$216,421 for the fiscal year ended June 30, 2005, and understated revenues and expenses of \$338,399 for the fiscal year ended June 30, 2006.

The office misclassified expenditures made under the Help America Vote Act. As a result, Grants from Federal Sources is understated by \$852,322, and Other Services, Supplies & Materials, Other Expenses,

and Grants from State Sources are overstated, by \$120,344, \$401,930, \$223,510, and \$106,538, respectively, for the fiscal year ended June 30, 2005. Grants from Federal Sources are understated, and Grants from State Sources are overstated, by \$4,677,545, for the fiscal year ended June 30, 2006.

In our opinion, except for the effect of the matters discussed in the preceding two paragraphs, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances/property held in trust of the office for each of the fiscal years ended June 30, 2006 and 2005, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

*/s/ James Gillett*

James Gillett, CPA  
Deputy Legislative Auditor

September 13, 2006

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	Federal Special Revenue Fund	Enterprise Fund
FUND BALANCE: July 1, 2005	\$ <u>5,526,096</u>	\$ <u>3,103,735</u>
ADDITIONS		
Budgeted Revenues & Transfers-In	7,895,224	3,990,859
Nonbudgeted Revenues & Transfers-In	26	220
Prior Year Revenues & Transfers-In Adjustments		15,184
Total Additions	<u>7,895,250</u>	<u>4,006,263</u>
REDUCTIONS		
Budgeted Expenditures & Transfers-Out	8,302,299	3,061,544
Nonbudgeted Expenditures & Transfers-Out		153,149
Prior Year Expenditures & Transfers-Out Adjustments		1,519
Total Reductions	<u>8,302,299</u>	<u>3,216,212</u>
FUND BALANCE: June 30, 2006	\$ <u><u>5,119,047</u></u>	\$ <u><u>3,893,786</u></u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST  
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	Federal Special Revenue Fund	Enterprise Fund	Agency Fund
FUND BALANCE: July 1, 2004	\$ <u>7,745,332</u>	\$ <u>2,516,190</u>	\$ <u>0</u>
ADDITIONS			
Budgeted Revenues & Transfers-In	275,885	3,616,418	
Prior Year Revenues & Transfers-In Adjustments		128,304	
Direct Entries to Fund Balance		(4,230)	
Additions to Property Held in Trust			295
Total Additions	<u>275,885</u>	<u>3,740,492</u>	<u>295</u>
REDUCTIONS			
Budgeted Expenditures & Transfers-Out	2,501,891	3,111,957	
Nonbudgeted Expenditures & Transfers-Out	1,605	33,723	
Prior Year Expenditures & Transfers-Out Adjustments	(8,375)	7,267	
Reductions in Property Held in Trust			295
Total Reductions	<u>2,495,121</u>	<u>3,152,947</u>	<u>295</u>
FUND BALANCE: June 30, 2005	\$ <u><u>5,526,096</u></u>	\$ <u><u>3,103,735</u></u>	\$ <u><u>0</u></u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.



SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN  
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	<u>Federal Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Total</u>
TOTAL REVENUES & TRANSFERS-IN BY CLASS			
Taxes		\$ 212	\$ 212
Charges for Services		3,755,008	3,755,008
Investment Earnings	\$ 380,447	106,662	487,109
Sale of Documents, Merchandise and Property		111,191	111,191
Miscellaneous		33,190	33,190
Federal	7,514,803		7,514,803
Total Revenues & Transfers-In	<u>7,895,250</u>	<u>4,006,263</u>	<u>11,901,513</u>
Less: Nonbudgeted Revenues & Transfers-In	26	220	246
Prior Year Revenues & Transfers-In Adjustments	0	15,184	15,184
Actual Budgeted Revenues & Transfers-In	<u>7,895,224</u>	<u>3,990,859</u>	<u>11,886,083</u>
Estimated Revenues & Transfers-In	<u>7,160,000</u>	<u>3,338,567</u>	<u>10,498,567</u>
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ 735,224</u>	<u>\$ 652,292</u>	<u>\$ 1,387,516</u>
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS			
Charges for Services		\$ 610,352	610,352
Investment Earnings	\$ 320,421	86,654	407,075
Sale of Documents, Merchandise and Property		(2,816)	(2,816)
Miscellaneous		(41,898)	(41,898)
Federal	414,803		414,803
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ 735,224</u>	<u>\$ 652,292</u>	<u>\$ 1,387,516</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.  
Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN  
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	<u>Federal Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Total</u>
TOTAL REVENUES & TRANSFERS-IN BY CLASS			
Charges for Services		\$ 3,535,000	\$ 3,535,000
Investment Earnings	\$ 139,347	30,353	169,700
Sale of Documents, Merchandise and Property		99,926	99,926
Miscellaneous		76,897	76,897
Grants, Contracts, Donations and Abandonments		941	941
Other Financing Sources		1,605	1,605
Federal	136,538		136,538
Total Revenues & Transfers-In	<u>275,885</u>	<u>3,744,722</u>	<u>4,020,607</u>
Less: Prior Year Revenues & Transfers-In Adjustments		128,304	128,304
Actual Budgeted Revenues & Transfers-In	<u>275,885</u>	<u>3,616,418</u>	<u>3,892,303</u>
Estimated Revenues & Transfers-In	290,000	4,506,372	4,796,372
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ (14,115)</u>	<u>\$ (889,954)</u>	<u>\$ (904,069)</u>
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS			
Charges for Services		\$ (633,232)	\$ (633,232)
Investment Earnings	\$ 79,347	10,353	89,700
Sale of Documents, Merchandise and Property		(183,096)	(183,096)
Miscellaneous		(86,525)	(86,525)
Grants, Contracts, Donations and Abandonments		941	941
Other Financing Sources		1,605	1,605
Federal	(93,462)		(93,462)
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ (14,115)</u>	<u>\$ (889,954)</u>	<u>\$ (904,069)</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.  
Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT  
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	<u>Business and Government Services</u>
Personal Services	
Salaries	\$ 1,612,433
Employee Benefits	559,478
Personal Services-Other	8,584
Total	<u>2,180,495</u>
Operating Expenses	
Other Services	3,560,193
Supplies & Materials	188,471
Communications	176,227
Travel	141,132
Rent	186,805
Utilities	1,014
Repair & Maintenance	188,345
Other Expenses	205,926
Goods Purchased For Resale	12,358
Total	<u>4,660,471</u>
Grants	
From State Sources	<u>4,677,545</u>
Total	<u>4,677,545</u>
Total Expenditures & Transfers-Out	<u>\$ 11,518,511</u>

EXPENDITURES & TRANSFERS-OUT BY FUND

Federal Special Revenue Fund	\$ 8,302,299
Enterprise Fund	<u>3,216,212</u>
Total Expenditures & Transfers-Out	11,518,511
Less: Nonbudgeted Expenditures & Transfers-Out	153,149
Prior Year Expenditures & Transfers-Out Adjustments	1,519
Actual Budgeted Expenditures & Transfers-Out	11,363,843
Budget Authority	14,137,957
Unspent Budget Authority	<u>\$ 2,774,114</u>

UNSPENT BUDGET AUTHORITY BY FUND

Federal Special Revenue Fund	\$ 2,602,593
Enterprise Fund	<u>171,521</u>
Unspent Budget Authority	<u>\$ 2,774,114</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE  
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT  
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	<u>Business and Government Services</u>
Personal Services	
Salaries	\$ 1,554,705
Employee Benefits	520,542
Personal Services-Other	(35,671)
Total	<u>2,039,576</u>
Operating Expenses	
Other Services	1,691,595
Supplies & Materials	741,012
Communications	393,327
Travel	52,007
Rent	146,261
Utilities	1,732
Repair & Maintenance	18,643
Other Expenses	441,434
Goods Purchased For Resale	14,338
Total	<u>3,500,349</u>
Grants	
From State Sources	106,538
Total	<u>106,538</u>
Transfers	
Accounting Entity Transfers	1,605
Total	<u>1,605</u>
Total Expenditures & Transfers-Out	<u>\$ 5,648,068</u>
EXPENDITURES & TRANSFERS-OUT BY FUND	
Federal Special Revenue Fund	\$ 2,495,121
Enterprise Fund	3,152,947
Total Expenditures & Transfers-Out	<u>5,648,068</u>
Less: Nonbudgeted Expenditures & Transfers-Out	35,328
Prior Year Expenditures & Transfers-Out Adjustments	(1,108)
Actual Budgeted Expenditures & Transfers-Out	<u>5,613,848</u>
Budget Authority	11,339,784
Unspent Budget Authority	<u>\$ 5,725,936</u>
UNSPENT BUDGET AUTHORITY BY FUND	
Federal Special Revenue Fund	\$ 5,426,993
Enterprise Fund	298,943
Unspent Budget Authority	<u>\$ 5,725,936</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

# **The Office of the Secretary of State**

## **Notes to the Financial Schedules for the Two Fiscal Years Ended June 30, 2006**

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### **1. Summary of Significant Accounting Policies**

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#### **Basis of Accounting**

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The Office of the Secretary of State (office) uses the modified accrual basis of accounting, as defined by state accounting policy, for its governmental fund. In applying the modified accrual basis, the office records:

Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.

Expenditures for valid obligations when the department incurs the related liability, and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the office to record the cost of employees' annual and sick leave when used or paid.

The office uses accrual basis accounting for its proprietary and fiduciary funds. Under the accrual basis, as defined by state accounting policy, the office records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the office receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

#### **Basis of Presentation**

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The financial schedule format is in accordance with the policy of the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

## Notes to the Financial Schedules

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The office uses the following funds:

### **Governmental Fund Category**

**Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. The office’s Federal Special Revenue Funds include activity related to the Help America Vote Act, Election Reform Payments, and Election Assistance for Individuals with Disabilities.

### **Proprietary Fund Category**

**Enterprise Fund** – to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities’ cost of providing services, including capital costs, be recovered with fees and charges rather than with taxes of similar revenues. The office’s Enterprise Fund activities include business services, administrative rules, election filings, management services, information services, and records management services.

### **Fiduciary Fund Category**

**Agency Fund** – to account for resources held by the state in a custodial capacity. During fiscal year 2004-05, the office was using a Property Held in Trust Fund to record revenue collections prior to coding these amounts to the appropriate revenue accounts on SABHRS. The office discontinued use of this fund in fiscal year 2005-06.

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## **2. Federal Revenues**

In fiscal years 2002-03, and 2003-04, the office received \$5,000,000 and \$4,243,462, respectively, in federal HAVA revenues. The office used these funds to develop a statewide voter database, replace punch-card voting systems, and educate elections officials and the public regarding new voting procedures.

The beginning fund balance for the Federal Special Revenue Fund of \$7,745,332, as shown on the Schedule of Total Changes in Fund

## **Notes to the Financial Schedules**

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Balances and Property Held in Trust for the Fiscal Year Ended June 30, 2005 on page A-6, reflects federal HAVA revenues that were recognized, but not expended, as of June 30, 2004.

In October 2005, the office received its third installment of HAVA funds, in the amount of \$7,446,803, which shows as Federal revenues on the Schedule of Total Revenues and Transfers-In for the Fiscal Year Ended June 30, 2006 on page A-7. There was no HAVA funds received in the prior fiscal year.

## **Office Response**

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OFFICE OF THE SECRETARY OF STATE  
STATE OF MONTANA

RECEIVED

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LEGISLATIVE AUDIT DIV.

BRAD JOHNSON  
SECRETARY OF STATE



STATE CAPITOL BUILDING  
PO BOX 202801  
HELENA, MT 59620-2801

November 28, 2006

Mr. Scott Seacat  
Legislative Auditor  
Legislative Audit Division  
P.O. Box 201705  
Helena, Montana 59620-1705

Dear Mr. Seacat:

Thank you for the opportunity to respond to the financial compliance audit report on the Office of the Secretary of State for the two fiscal years ending June 30, 2006.

The financial compliance audit includes six recommendations. Our response to each recommendation is provided below.

*Recommendation #1: Record revenues and expenses associated with electronic business transactions in accordance with state accounting policy.*

Concur. This office has already met with Montana Interactive and established new protocol that will ensure that all revenues collected by Montana Interactive for electronic services provided by this office will be recorded as revenue received and amounts paid to Montana Interactive recorded as expenses of the office.

Montana Interactive has provided us with both the gross revenue and the associated expenses for each electronic service for each month of Fiscal Year 2007 and we will record each accordingly. In addition we have modified our budget for FY 2007 and established a budget for the FY 2008-2009 biennium that reflects the gross revenue received as well as the associated expenses. We believe actions we have taken fully satisfy this recommendation.

*Recommendation #2: Properly classify federal expenditures in accordance with state accounting policy.*

Concur. The office has submitted a request to establish needed spending authority for grants. After the request is approved, the office will record FY 2007 federal expenditures accordingly. The office will also review all expenses associated with federal funds to account for each in accordance with state accounting policy. Corrections will be made where appropriate.

*Recommendation #3: Provide the appropriate level of accounting expertise to its staff to ensure office transactions are properly recorded on the state's accounting system.*

Page B-3

Concur. This office has already established a new part time fiscal manager position that will be responsible for overseeing all budgeting and accounting activity in the office. The new fiscal manager began work on November 20, 2006. One of the priorities of the fiscal manager will be to identify and provide appropriate training to the accounting staff to ensure all office transactions are properly recorded on the state's accounting system.

The office has updated the job profiles for the accounting staff and implemented an individualized performance appraisal tool with measurable objectives to ensure accuracy and compliance with state policies.

*Recommendation #4: Provide training and develop procedures to properly administer its federal programs.*

Concur. One of the duties of the new fiscal manager will be to identify a variety of areas related to accounting and fiscal management where additional training is needed. The fiscal manager will also work with the Deputy for Administrative Rules and Management Services to establish procedures to ensure the proper administration of our federal programs.

This office has worked closely with the Montana Advocacy Program (MAP) to provide improved opportunities for individuals with disabilities to vote. The office is working with MAP to review the requirements of the federal grants and to retroactively establish a contract that will ensure all federal grant requirements are satisfied.

During the audit it was determined that the office has double reported expenses of approximately \$131,000 to the Election Assistance Commission. This office will review and reconcile all expenditures of federal funds and will file an amended report with the federal Election Assistance Commission. In addition, the office will provide training to staff on other areas that may be noted during the review.

While this office is not able to provide adequate documentation for informational advertisements that were purchased in FY 2004-05, we have followed state procurement rules and procedures for the various purchases made since the current administration assumed office. We will continue to provide staff guidance in the area of state procurement policies.

*Recommendation #5: Comply with state law by ensuring that fees charged for its business services reflect the cost of providing those services.*

Concur. Because this office operates as an enterprise fund we have believed this provided some flexibility in our capability to plan ahead for major capital investment projects in the information technology (IT) arena. During the audit this office identified four individual IT projects that will be implemented this year and during the next biennium. The implementation of these projects will reduce our enterprise fund STIP account balance significantly. However, we now recognize that while this office has some flexibility in

Mr. Scott Seacat  
Page 3  
November 28, 2006

managing revenues to match expenses, there may be some question as to how much flexibility the law allows.

To ensure that the fees charged by this office are commensurate with the costs, and to reduce the current balance in our enterprise fund STIP account this office will make some modifications to its FY 2007 budget and will plan to do the same for the FY 2008-09 biennium.

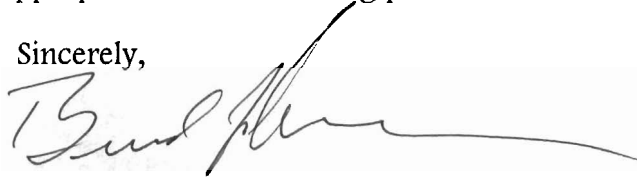
The passage of the Help America Vote Act (HAVA) has brought with it significant responsibilities for state and local government. These responsibilities will also have long term financial implications for the state and local governments. Beginning in FY 2007 this office will shift the cost of some existing operations from federal funds to our enterprise fund. Among the costs to be shifted will be those associated with the Department of Administration hosting the statewide voter registration database, and for providing voter registration database help desk support to county election offices. This office will retain federal funds for use in the replacement of hardware and software associated with the statewide voter registration database as well as for providing accessibility grants to counties and for voter outreach. We believe this shift in funding operations in this office will begin to bring our costs and fee structure more in line. This office will also initiate a comprehensive analysis of our fee structure during Fiscal Year 2007.

*Recommendation #6: Comply with state law by providing the legislature information reporting state and UCC rule discrepancies.*

Concur. This office has identified several areas where the Montana Code Annotated (MCA) and the Administrative Rules of Montana (ARM) are not in harmony with the model rules adopted for the Uniform Commercial Code. A report detailing these differences will be provided to the legislature by the end of this calendar year.

I would like to thank the staff of the Legislative Audit Division for their professionalism and cooperation during this audit. This audit has been a learning experience for many in this office and we sincerely appreciate the efforts of the legislative auditor's staff to help increase our knowledge and understanding of appropriate state accounting practices.

Sincerely,



BRAD JOHNSON  
Secretary of State

BJ:sba